

California Fair Political Practices Commission

MEMORANDUM

To: Chairman Randolph, Commissioners Blair, Downey, Karlan, and Knox

From: Natalie Bocanegra, Commission Staff Counsel
Luisa Menchaca, General Counsel

Re: Personal Loans (§ 85307) - Pre-notice Discussion of Proposed Amendments to Regulation 18530.8

Date: July 23, 2004

I. EXECUTIVE SUMMARY

Section 85307 of the Political Reform Act (“Act”)¹ currently covers two primary issues - extensions of credit² and personal loans. Whether and how subdivisions (a) and (b) of this section are read together has been the subject of discussion at several Commission meetings since 2001.³ In light of the recent litigation and pending legislation pertaining to the \$100,000 limit of section 85307, the Commission is asked whether it wishes to re-examine the Commission’s prior interpretation regarding the limit. Proposed regulatory language amending regulation 18530.8 and corresponding decision points are presented to the Commission as follows:

- **Decision Point 1:** Should the Commission amend subdivision (c) of regulation 18530.8 to provide that the \$100,000 personal loan limit of section 85307 is applicable to proceeds of a loan made to a candidate by a commercial lending institution for which the candidate is personally liable?

¹ All references are to the Government Code, unless otherwise noted.

² As described in the “Proposition 34 Retrospective – Proposed Regulatory Refinements” approved by the Commission in December 2003, this regulatory project also pertains to determining the length of time that may pass before an extension of credit becomes a contribution. Since the policy discussion on extensions of credit may be significantly altered as a result of any amendment to section 85307 or regulation 18530.8, staff plans to present discussion of this issue at a future Commission meeting.

³ Commission staff held an Interested Persons’ meeting in May 2001 to discuss section 85307. A proposed regulation relating to extensions of credit (regulation 18530.7) was presented for Commission consideration at its September 2001 meeting, as well as proposed regulation 18530.8, relating to contribution limits. The Commission deferred consideration of regulation 18530.7 but moved forward with a second pre-notice discussion of regulation 18530.8 in November 2001 and adoption of that regulation in January 2002.

- **Decision Point 2:** Should the Commission describe by regulation when it is that loans are made “by a commercial lending institution in the lender’s regular course of business on terms available to members of the general public?”

Pending legislation may amend section 85307 to provide that state candidates are subject to a \$100,000 personal loan limit under any circumstances. However, staff recommends that the Commission proceed with determining whether regulation 18530.8(c) should be amended to provide that the \$100,000 limit of section 85307 applies to loans from commercial lending institutions. Any proposed amendment could be noticed for adoption at the October 2004 Commission meeting, at which time the Commission will know the outcome of the pending legislation. Staff does not offer a specific recommendation on whether to amend the regulation, but this memo will provide the analytical framework for reaching a determination on this matter. In addition, staff further recommends that no action be taken at this time to define the term “by a commercial lending institution in the lender’s regular course of business on terms available to members of the general public.”

II. PERSONAL LOAN LIMIT

A. Background

Section 85307, which was enacted by Proposition 34, states:

“(a) The provisions of this article regarding loans apply to extensions of credit, but do not apply to loans made to a candidate by a commercial lending institution in the lender’s regular course of business on terms available to members of the general public for which the candidate is personally liable.

(b) A candidate for elective state office may not personally loan to his or her campaign an amount, the outstanding balance of which exceeds one hundred thousand dollars (\$100,000). A candidate may not charge interest on any loan he or she made to his or her campaign.”

Pursuant to section 85307, a candidate for elective state office may not personally loan to his or her campaign an amount, the outstanding balance of which exceeds \$100,000. In 2001, the Commission interpreted this section to mean that the \$100,000 limit does not “apply to loans made to a candidate by a commercial lending institution in the lender’s regular course of business on terms available to members of the general public for which the candidate is personally liable.”

Specifically, regulation 18530.8 provides:

“(a) Any personal loan made before January 1, 2001, by a candidate for elective state office does not count toward the

\$100,000 loan limit of subdivision (b) of Government Code section 85307.

(b) For purposes of subdivision (b) of Government Code section 85307 and this regulation, ‘campaign’ encompasses both the primary and general elections or special and special runoff elections for a specific term of elective state office. ‘Campaign’ includes any of the candidate’s controlled committees formed for the purpose of seeking that elective state office and all committees formed for the purpose of supporting the candidate’s candidacy for that elective state office.

(c) The proceeds of a loan made to a candidate by a commercial lending institution for which the candidate is personally liable, pursuant to the terms of subdivision (a) of Government Code section 85307, which the candidate then lends to his or her campaign do not count toward the \$100,000 loan limit of subdivision (b) of Government Code section 85307.

(d) A candidate may make a series of personal loans to his or her campaign as long as the outstanding balance does not exceed \$100,000 at the time of making the loans. If a candidate’s personal loan balance has reached the \$100,000 limit, the loan balance must be reduced before the candidate may make any additional loans to his or her campaign.”

Since adoption of regulation 18530.8, there have been recent developments involving interpretation of section 85307. In January 2004, in *Camp v. Schwarzenegger*, Sacramento Superior Court, Case No. 03AS05478, Judge Loren E. McMaster ruled in a case challenging a \$4 million loan that gubernatorial candidate Arnold Schwarzenegger made to his campaign. Judge McMaster ruled on two issues in the case: whether the loan was made on terms available to members of the general public, and whether the candidate could loan his campaign more than \$100,000. The court ruled that the loan was made on terms available to members of the general public, despite the fact that only a small percentage of the public could actually take advantage of those terms due to their personal financial status. The court further held that section 85307(b) prohibits a candidate from personally loaning his or her campaign account more than \$100,000, regardless of the fact that the original source of the funds used by the candidate to fund the loan to his or her campaign is a commercial loan to the candidate which meets the requirements of section 85307(a). This latter conclusion conflicts with regulation 18530.8(c). However, the holding of the court does not have application beyond the parties involved since the matter was not appealed.

In response to *Camp v. Schwarzenegger*, AB 2842 (Leno) (Attachment 1) and SB 1449 (Johnson) (Attachment 1) were introduced to codify the ruling. As the June 28, 2004, Senate Floor Analysis of AB 2842 explains:

“Despite this ruling, legislative candidates continue to obtain these

type of loans. In fact, five legislative candidates for the November 2004 election took out bank loans in excess of the \$100,000 limit. One of these loans was taken out after the Superior Court's ruling.

Since the Superior Court ruling does not carry the force of law, the Legislature must act immediately to close this loophole."

Both bills generally provide that the proceeds of a loan obtained by a candidate from a commercial lending institution and loaned by the candidate to his or her campaign are subject to the \$100,000 personal loan limitation. AB 2842, in contrast to SB 1449, deletes section 85307(a). Both bills are nearing the end of the legislative process and have been moving with little opposition. The Commission has a support position on SB 1449, and AB 2842 is fully discussed in the Commission's legislative report.

Decision Point 1: Should the Commission amend regulation 18530.8 to provide that the \$100,000 personal loan limit is applicable to proceeds of a loan made to a candidate by a commercial lending institution for which the candidate is personally liable?

Regulation 18530.8(c) currently provides that if a candidate receives a loan from a commercial lending institution for which the candidate is personally liable for the loan and then loans the funds to his or her campaign, those funds *do not* count toward the \$100,000 loan limit of subdivision (b) of Government Code section 85307. (Regulation 18530.8 (c).)

Specifically, the Commission is asked whether this regulation should be modified to provide that proceeds of a loan made by a commercial lending institution in this context do count toward the \$100,000 loan limit.

In reviewing the interpretation of section 85307, it is important to keep in mind the following rules that apply to loans and personal funds:

- Because a loan is considered a contribution, loans are ordinarily subject to the contribution limits set forth in the Act. (Section 82015.)
- A loan is not a contribution if the loan is received from a commercial lending institution in the ordinary course of business. (Section 84216(a).)
- A loan is not a contribution if it is clear from the surrounding circumstances that it is not made for political purposes.
- A loan from a candidate's personal funds to his or her campaign is a contribution to the candidate's campaign, but it is not subject to the contribution limits of section 85301 because those limits do not apply to a candidate's contribution of his or her own personal funds. (Section 85301(d).) Instead, with respect to personal loans, section 85307(b) imposes a limit

of \$100,000 on the outstanding balance of the loan that a candidate may make to his or her campaign.

Section 85307(a) provides that “[t]he provisions of this article regarding loans ... do not apply to loans made to a candidate by a commercial lending institution in the lender’s regular course of business on terms available to members of the general public for which the candidate is personally liable.” This section applies to any candidate. In contrast, subdivision (b), which contains the \$100,000 limit on the outstanding balance, is limited in its application to candidates for elective state office. The question then arises whether the \$100,000 limit imposed by section 85307(b) applies to the proceeds of a bank loan made to a candidate and then loaned by a candidate to his or her committee.

B. Two Reasonable Interpretations

Loans from Commercial Lending Institutions Do Not Count: After three Commission meetings and public input, the Commission determined that while the language “[t]he provisions of this article regarding loans” found in section 85307(a) refers to more than just section 85307(b), the term “loan” is not found elsewhere in the article. Therefore, only section 85307(b) can be included within its scope. This leads to the conclusion that section 85307(b) cannot apply to loans obtained by a candidate from commercial lending institutions in the ordinary course of business.

As mentioned above, under section 84216, a loan from a commercial lending institution to a candidate in the ordinary course of business is not a contribution. Arguably, then, section 85307 cannot be read to impose a contribution limit on a loan from a commercial lending institution. Under this reading of section 85307(a), the personal loan \$100,000 limit of section 85307(b) is inapplicable to loans to a candidate from a commercial lending institution.

In summary, by analyzing the process of a candidate taking a loan from a commercial lending institution and lending it to his or her campaign as *one* transaction instead of two separate transactions, bank loan proceeds are not subject to the limits imposed by section 85307(b). The Commission adopted this interpretation at its January 15, 2002, meeting, and it is reflected in regulation 18530.8(c).

Loans from Commercial Lending Institutions Do Count: Another possible interpretation of the statute is to view the loan from the bank and the candidate’s use of those funds as separate transactions even if arising out of the same set of facts, thereby analyzing subdivisions (a) and (b) separately.

Pursuant to section 84216, a loan *to a candidate* from a commercial lending institution in the ordinary course of business is not a contribution to the candidate’s campaign. Pursuant to section 85307(b), a loan *from a candidate* to his or her campaign is limited to an outstanding balance of \$100,000 at any given time. Therefore, by analyzing the process as two separate transactions, it is possible to conclude that when a commercial lending institution makes a loan

to a candidate, the funds become an asset of the candidate in the first transaction. In the second transaction, the candidate converts the funds he or she received from the bank, and *the candidate loans the funds to his or her campaign*, thus making the funds subject to section 85307(b).⁴

In addition, section 85307(a) provides that extensions of credit, which may be considered loans will be deemed contributions subject to the limits of sections 85301 and 85302. This conclusion is reached by interpreting the term “article” in section 85307(a) to apply to contributions (as referenced in sections 85301 and 85302 and in other sections of the article), which include loans. In other words, section 85307(a) exists for the purpose of providing a contribution limitation on extensions of credit and extending the reporting rationale of section 84216 to Chapter 5, relating to contribution limits, while section 85307(b) exists to establish a \$100,000 limitation on a candidate’s use of his or her own funds, regardless of the source of the funds.

Another argument in support of this approach is that if the loan is not considered a contribution of a candidate’s personal funds, the voluntary expenditure limits would never be lifted as long as a candidate used monies obtained through a bank loan. (Section 85402.)

C. Statutory Construction

Although the Commission rejected the latter approach in January of 2002, based on language of section 85307 with definitions drawn from other statutory provisions of the Act and past Commission advice, section 85307 is capable of more than one reasonable interpretation as explained below.

In *Camp v. Schwarzenegger*, the court found that regulation 18530.8(c) was an “erroneous and unreasonable construction” of section 85307. (*Camp, supra*, 20.) The court relied on its interpretation of section 85307(a) which included the conclusion that the statute is “not reasonably susceptible of a different interpretation.” (*Camp, supra*, 11 – 20.) However, the statute is capable of an alternate interpretation.

“In statutory construction cases, a court’s fundamental task is to ascertain the intent of the lawmakers so as to effectuate the purpose of the statute.” *Estate of Griswold*, No. S087881, 2001 WL 694081, at *3 (Cal. Sup. Ct., June 21, 2001). The proper approach to construction of a statute is succinctly outlined as follows:

“We begin by examining the statutory language, giving the words their usual and ordinary meaning. [Citations omitted.] If the terms of the statute are unambiguous, we presume the lawmakers meant what they said, and the plain meaning of the language governs. [Citations omitted.] If there is ambiguity, however, we may then

⁴ If the Commission adopts this interpretation, staff recommends both the bank and the candidate be reported as the sources of the loan. (See regulation 18530.8(c), Attachment 2.)

look to extrinsic sources, including the ostensible objects to be achieved and the legislative history. [Citation omitted.] In such cases, we select the construction that comports most closely with the apparent intent of the Legislature, with a view of promoting rather than defeating the general purpose of the statute, and avoid an interpretation that would lead to absurd consequences.” [Citations and internal quotation marks omitted.]

Estate of Griswold, supra.

If the statute has an unambiguous meaning, then “plain meaning” is applied and the interpretational task requires nothing further. (*People v. Camarillo*, 84 Cal.App.4th 1386, 1391 (2000).) When a statute is “ambiguous” (that is, capable of more than one reasonable interpretation), it is necessary to turn for assistance in interpretation to “extrinsic sources including the ostensible objects to be achieved and the legislative history.” (*Estate of Griswold, supra*, 2001 WL 694081, at *3.)

In construing the meaning of section 85307, it is first necessary to examine the statutory language, giving the words their usual and ordinary sense, to determine whether the statute has a clear, unambiguous meaning. Prior staff analysis of section 85307(b) was conducted under the assumption that this statute is ambiguous. (Staff memoranda: “Proposition 34 Regulations: Personal Loans (§ 85307) – Second Pre-Notice Discussion of Proposed Regulation 18530.8,” October 25, 2001; “Proposition 34 Regulations: Personal Loans (§ 85307) – Adoption of Proposed Regulation 18530.8,” December 27, 2001.) Staff believes that there is sufficient ambiguity in section 85307 to consider extrinsic sources. As articulated above, when a statute is capable of more than one reasonable interpretation, it is appropriate to turn to extrinsic sources for assistance. As a result, the Commission has, as an option, the ability to reaffirm its adoption of regulation 18530.8(c) or to alter its interpretation.

On this point, although Proposition 34 was a legislative initiative, the Legislature’s intent in drafting section 85307 is not relevant since there is no indication that the voters had any idea of the drafters’ intent. (*Taxpayers to Limit Campaign Spending v. Fair Political Practices Commission*, 51 Cal.3d 744, 764, n. 10 (1990), noting that the motive or purpose of the drafters is not relevant since the opinion does not represent the intent of the electorate.) When seeking to ascertain the voters’ intent, the normal procedure is to review the voter information pamphlet which is distributed to all registered voters in the state. The Official Voter Information Guide for the November 2000 election (containing the official summary of Proposition 34, as well as the ballot arguments for and against the measure), at the Analysis by the Legislative Analyst section states the following:

“Under this measure, candidates would be allowed to give unlimited amounts of their own money to their campaigns. However, the amount candidates could loan to their campaigns

would be limited to \$100,000 and the earning of interest on any such loan would be prohibited.”

(Official Voter Information Guide, November 2000 Election, pg. 14.)

Perhaps more helpful to the present analysis, however, is the following statement regarding the subject matter of section 85307(b), which is found in the Arguments in Favor of Proposition 34, in the Official Voter Information Guide:

“PROPOSITION 34 CLOSES LOOPHOLES FOR WEALTHY CANDIDATES

Wealthy candidates can loan their campaigns more than \$100,000 then have special interests repay their loans. Proposition 34 closes this loophole.”

Ultimately, when adopting regulation 18530.8, the Commission determined that while the ballot pamphlet addressed limitations by candidates as to their own funds, it did not directly address the issue of bank loans. (Commission minutes of January 15, 2002.) In order to give subdivision (a) meaning, the Commission weighed the evidence in favor of reading subdivisions (a) and (b) together. The Commission recognized that “this may be a regulation that will need legislation to fix.” (Chairman Getman, Commission meeting minutes January 15, 2002.)

Applying regulation 18530.8 to proceeds of a loan made to a candidate by a commercial lending institution for which the candidate is personally liable could be viewed as being supported by the Arguments in Favor of Proposition 34, from the Official Voter Information Guide, quoted above. According to the Argument, one of the goals of Proposition 34 was to discourage the wealthy candidate from being able to loan himself or herself more than \$100,000, and then obtain contributions to pay off the loan. Further, it may be argued that the “loophole” referred to in the ballot pamphlet argument, by which wealthy candidates loan themselves funds in excess of \$100,000 from commercial lending institutions has been sufficiently closed by the imposition of section 85307.

The issue before the Commission, if it determines it should amend regulation 18530.8 now, is whether the Commission wishes to weigh the policy issues in favor of reading subdivisions (a) and (b) separately, as discussed above. A proposed amendment that would modify regulation 18530.8 to take an interpretation consistent with that in *Camp v. Schwarzenegger* is presented to the Commission for discussion. (Attachment 2.)

Staff Recommendation: If enacted, Assembly Bill 2842 or Senate Bill 1449 will provide a legislative amendment that would remove any ambiguity in the current statute. Nevertheless, while recognizing that pending legislation may determine the \$100,000 loan limit issue, staff recommends that the Commission proceed with determining whether regulation 18530.8(c) should be amended. If the Commission believes that the \$100,000 limit should be

applied and that a regulatory approach is proper, the proposed regulatory amendment could be noticed for adoption at the October 2004 Commission meeting, at which time the Commission will also know the outcome of the pending legislation. Making a decision on this amendment would help to give candidates notice of the Commission's view on this matter, given the recent litigation. However, if the Commission believes, as it did in 2001, that only a legislative amendment would be the proper approach to apply the \$100,000 limit, the Commission should not alter regulation 18530.8 at this time. Because there is legal validity to either supporting or opposing amendment to regulation 18530.8, staff does not offer a recommendation on this issue but rather leaves this policy decision to the Commission.

III. FURTHER REGULATORY DEFINITION

Decision Point 2: Should the Commission describe by regulation when it is that loans are made "by a commercial lending institution in the lender's regular course of business on terms available to members of the general public for which the candidate is personally liable?"

In *Camp v. Schwarzenegger*, the superior court also addressed the issue of whether a bank loan obtained by gubernatorial candidate Arnold Schwarzenegger at prime totaling over \$4 million was a loan "made to a candidate by a commercial lending institution in the lender's regular course of business on terms available to members of the general public." The court decided that the subject loan was made on "terms available to members of the general public" as that phrase is used in section 85307. The court stated:

"Based upon the undisputed facts, Defendants have demonstrated that the size, terms, duration, and processing of the loan made by CNB to Candidate Schwarzenegger were not aberrant from CNB's regular course of business, and that CNB made many similar (or even more favorable and larger loans) to other individual members of the general public within the preceding 6 month period."

The plaintiff in this case had argued that the loan was not available to "members of the general public" because a significant and diverse segment of the population could not qualify to receive the same loan. The plaintiff's approach, rejected by the court, is similar to the one employed by the Commission in *Russel* (1975) 1 FPPC Ops. 191, in determining whether a discount rate was made available to "members of the public." In this opinion, the Commission concluded that the statutory language using this term did not require that the discount be made available to all members of the public, but instead implied that the discount must be offered on a "uniform basis to a diverse group." Specifically, the Commission considered whether the group receiving the discount was a "large and heterogeneous assortment of individuals."

The Commission may wish to describe when it is that bank loans are excluded from being counted toward the \$100,000 personal loan limit. Proposed language could be based on analysis provided by the *Russel* opinion as follows:

“(e) A loan made in a lender’s regular course of business on terms available to members of the general public is a loan with a size, duration, terms, and processing which are [regularly available to] [regularly approved for] [offered on a uniform basis to] a [significant] [large] and [diverse] [heterogeneous] group of the lender’s customers.”

Staff Recommendation: Staff believes that if loans from a commercial lending institution are to be counted toward the personal loan limit, the Commission does not need to further describe when it is that actual loans are those made “by a commercial lending institution in the lender’s regular course of business on terms available to members of the general public.” However, further description may be beneficial if these types of loans are not counted so that this exemption is narrowly tailored sufficiently to carry out the purposes of Proposition 34. Staff recommends that no action be taken at this time to define the term “by a commercial lending institution in the lender’s regular course of business on terms available to members of the general public” because the need for defining this term is tied to the outcome of legislation amending, or alternatively the Commission’s ultimate interpretation of, section 85307. However, staff requests permission to revisit this issue should a future need arise from the Legislature’s or Commission’s action pertaining to section 85307.

Attachments

Attachment 1 – AB 2842 and SB 1449

Attachment 2 – Proposed amendments to regulation 18530.8